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IN THE

Supreme Court of the United States

OCTOBER TERM, 1933.

No.....

SEWELL LEE AVERY,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

SEWELL L. AVERY,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT, AND SUPPORTING BRIEF.

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Your petitioner respectfully prays for a writ of *certiorari* to review the judgments of the Circuit Court of Appeals for the Seventh Circuit, affirming certain decisions of the United States Board of Tax

Appeals, which said decisions confirmed deficiencies against petitioner for income taxes for the calendar years 1924 and 1929.

The deficiencies resulted from the holding that certain corporate dividends were taxable to petitioner in the years 1924 and 1929, respectively, rather than in 1925 and 1930, respectively, the years in which the dividends in question were reported by the petitioner.

QUESTIONS PRESENTED.

The same question is involved as to each of the years 1924 and 1925.

As to 1924—

> Were the dividends of $266,490.10 income for 1924 because of the fact that they were declared and payable in that year or were they income for 1925 as claimed by Petitioner because of the fact that the dividend checks were not actually received by him until 1925?

As to 1929—

> Were the dividends of $48,984 income for 1929 because of the fact that they were declared and payable in that year, or were they income for 1930 as claimed by Petitioner because of the fact that the dividend checks were not actually received by him until 1930?

Petitioner claims that the dividends in question were not received by him, within the meaning of the applicable provisions of the Revenue Acts, until the dividends actually came to hand through receipt of the dividend checks. Respondent, on the other hand, claims that the dividends were "received" by petitioner in the years in which the dividends were respectively declared and by their terms payable.

The Board of Tax Appeals sustained the Commissioner, and was in turn sustained by the court below. The Board in its opinion discussed the question at length. (Tr. 23-33.)

The opinion below (Tr. 87) attempts no extended discussion of the legal points involved.

STATEMENT.

Petitioner is a stockholder of United States Gypsum Company. In November, 1924, that company declared a dividend upon its stock, payable on or before December 31, 1924 to stockholders of record at the close of business on December 5, 1924 (Tr. 17). Dividend checks were mailed out to the stockholders on December 31, 1924, excepting that in the case of about fifty employees at the principal office of the company in Chicago, including Petitioner, the checks were held by the treasurer and not delivered until January 2, 1925. Petitioner, therefore received his dividends checks aggregating $266,490.10 on January 2, 1925 (Tr. 19-20).

These dividends were reported by Petitioner as income for the year 1925 (Tr. 17).

The practice followed by the company in sending out its dividend checks appears in detail in the record (pp. 20-22; 26-27) and will not be repeated here. The purpose and intent of the company was to preclude receipt by any stockholder of his dividends prior to January of the succeeding calendar year in each case.

In November, 1925, the company declared further dividends, payable on or before December 31, 1925 to stockholders of record at the close of business on

December 5, 1925 (Tr. 17-18). The dividends were paid in the same manner as in the case of the 1924 dividends, and Petitioner accordingly received his dividend checks on January 2, 1926 aggregating $161,511.70 (Tr. 19-20). These dividends were included in Petitioner's 1926 return (Tr. 17-18).

In November, 1926, a dividend was declared, payable on or before December 31, 1926 to stockholders of record at the close of business on December 4, 1926. The dividend was paid in the same manner, Petitioner receiving his dividend checks amounting to $140,117.30 on January 2, 1927 (Tr. 19-20), which dividends were included in Petitioner's 1927 return (Tr. 18).

In November, 1928, a dividend was declared, payable on or before December 31, 1928 to stockholders of record at the close of business on December 15, 1928 (Tr. 19). The dividend was paid in the same manner as before and Petitioner received dividend checks amounting to $32,656 on January 2, 1929 (Tr. 19-20) which were included in his 1929 return (Tr. 19).

In November, 1929, a dividend was declared, payable on or before December 31, 1929 to stockholders of record at the close of business on December 14, 1929 (Tr. 19). The dividend was paid in the same manner as before, Petitioner receiving checks aggregating $48,984 on January 2, 1930 (Tr. 19-20), which dividends were included in his 1930 return (Tr. 19).

Treating in each case the dividends in question as income for the year in which they were respectively declared and made payable and not as income for the year in which the dividend checks were actually

received by Petitioner, respondent increased Petitioner's 1924 income by the amount of the said dividends of $266,490.10; decreased his 1925 income by the amount of said last mentioned dividends and increased it by the amount of the said dividends of $161,511.70; decreased his 1926 income by the amount of the last mentioned dividends and increased it by the amount of the said dividends of $140,117.30 (Tr. 9-12); and decreased Petitioner's 1929 income by the amount of the said dividends of $32,656 and increased it by the amount of the said dividends of $48,984 (Tr. 50).

The following table shows the years in which the dividends were reported by Petitioner, together with the years in which the respondent claims they should be reported:

Year	Returns as Made	Returns as Adjusted
1924	.....	$266,490.10
1925	$266,490.10	161,511.70
1926	161,511.70	140,117.30
1927	140,117.30	.....
1928	.....	32,656.00
1929	32,656.00	48,984.00
1930	48,984.00	.....

The foregoing adjustments resulted in the asserted deficiency of $101,269.27 for 1924, [No. 5029 below] overassessments of $20,995.68 and $3,791.26 for 1925 and 1926, respectively, and the asserted deficiency of $2,658.13 for 1929. [No. 5030 below.]

The 1924 and 1929 deficiencies were appealed to the Board of Tax Appeals and were there affirmed. (Tr. 33, 63).

Both cases were appealed to the court below and

were there affirmed. The two cases were consolidated before the Board and were again consolidated in the court below and heard upon a single printed transcript (Tr. 81).

This petition is presented as to both cases.

The facts were mostly stipulated, and in any event were not disputed. They are set out in full in the record (Tr. 16-23).

REASONS FOR GRANTING THE WRIT.

1. The decision of the court below is in conflict with the decisions of other Circuit Courts of Appeal upon the same question. There is complete lack of uniformity between the various circuits on the point.

2. The court below has decided an important question of Federal law, involving the construction and application of the Revenue Acts of 1924 and 1928, which has not been, but should be, settled by this court.

These reasons will be elaborated upon in the brief.

It is respectfully submitted, therefore, that the writ of certiorari herein prayed issue for the reasons urged.

JOHN E. MACLEISH,
LELAND K. NEEVES,
Counsel for Petitioner.

BRIEF IN SUPPORT OF PETITION.

OPINIONS BELOW.

The opinion of the Circuit Court of Appeals for the Seventh Circuit is reported in 67 Fed. (2d) 310, and appears on pages 87-89 of the transcript. The opinion of the Board of Tax Appeals appears in the transcript at pages 23-33, and is otherwise unreported.

JURISDICTION.

The judgment of the Circuit Court of Appeals was entered on October 26, 1933 (Tr. 89, 99). Petition for rehearing was denied on November 21, 1933 (Tr. 90, 100).

Jurisdiction is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925. (Sec. 347, ch. 9, Title 28, U. S. C. A.)

QUESTIONS PRESENTED.

The questions presented are stated in the petition (*ante*, p. 2).

STATUTES INVOLVED.

The pertinent portions of the statutes involved are as follows:

Section 213 (a) of the Revenue Act of 1924 provides:

> "The term 'gross income' includes gains, profits and income derived from salaries, wages or

compensation for personal services * * *; also from interest, rent, dividends, securities * * * or gains or profits and income derived from any source whatever. The amount of all such items shall be included in the gross income for the taxable year in which received by the taxpayer, unless under methods of accounting permitted under Subdivision (b) of Section 212 any such amounts are to be properly accounted for as of a different period."

Section 212 (b) of the 1924 act provides:

"The net income shall be computed upon the basis of the taxpayer's annual accounting period (fiscal year or calendar year, as the case may be) in accordance with the methods of accounting regularly employed in keeping the books of such taxpayer, but if no such method of accounting has been so employed, or if the method employed does not clearly reflect the income, the computation shall be made in accordance with such method as in the opinion of the Commissioner does clearly reflect the income. * * *"

Section 22 of the Revenue Act of 1928 provides:

"'Gross income' includes gains, profits and income derived from salaries, wages or compensation for personal service, of whatever kind and in whatever form paid * * *; also from interest, rent, dividends, securities * * * or gains or profits on income derived from any source whatever."

Section 42 of the 1928 Act provides:

"The amount of all items of gross income shall be included in the gross income for the taxable year in which received by the taxpayer, unless under methods of accounting permitted under Section 41 any such amounts are to be properly accounted for as of a different period."

Section 41 of the 1928 Act is substantially the same as Section 212 (b) of the 1924 Act.

The pertinent provisions of the Regulations issued under the various Acts, appear in the Appendix (*Infra*, pp. 29-36).

STATEMENT.

A statement of the case is in the petition (*Ante*, p. 3).

ERRORS TO BE ASSIGNED.

I. THE CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT ERRED IN AFFIRMING THE JUDGMENT OF THE BOARD OF TAX APPEALS IN EACH OF THE TWO CASES.

II. THE CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT ERRED IN NOT HOLDING THAT THE DIVIDENDS HEREINBEFORE MENTIONED OF $244,690.10 AND $48,984, WERE INCOME FOR 1925 AND 1930 RESPECTIVELY, THE YEARS WHEN SAID DIVIDENDS WERE IN FACT RECEIVED BY PETITIONER.

III. THE CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT ERRED IN NOT REVERSING THE JUDGMENT AND FINDING OF THE BOARD OF TAX APPEALS IN EACH OF THE TWO CASES.

SUMMARY OF ARGUMENT.

I. Both the 1924 and 1928 Revenue Acts provide that all items of gross income, including dividends, shall be included in the taxpayer's gross income for the taxable period in which received by him, excepting only where other methods of accounting are permissible. This latter exception is not in-

volved in the instant case. The question here to be decided is whether certain dividends were taxable income to petitioner in 1924 and 1929, respectively, or in 1925 and 1930, respectively. The Commissioner claims that the dividends are taxable for the years first mentioned. The petitioner claims that they are taxable for the years last mentioned. Neither the 1924 nor the 1928 statute makes any distinction in reporting income as between dividends and all other items of income. These Acts differ in this regard from the 1921 Act which declared a special rule in Section 201(e) of that Act applicable to dividends alone and which Act in Section 213(a) expressly excepted dividends from the criterion of receipt, which criterion applied to all other items of income.

The dividends here involved were declared and made payable in 1924 and 1929, respectively. Dividend checks were sent out by the corporation on December 31st of each of the two years 1924 and 1929, which checks did not come into the possession of the petitioner until January 2, 1925 and 1930, respectively. Petitioner claims that the dividends were therefore "received" by him in 1925 and 1930, respectively, and should be reported accordingly. He did in fact report the dividends for those years. The Commissioner claims that the dividends were constructively received by petitioner in 1924 and 1929, respectively, because of the fact that the dividends were declared and made payable in those years. His contention is founded upon certain regulations issued by him to the effect that dividends are to be regarded as constructively received when made unqualifiedly subject to the taxpayer's demand.

These regulations adopted in substance the special provisions of Section 201(e) of the 1921 Act.

The word "received" in the 1924 and 1928 Acts is free from ambiguity and admits of no interpretation as is here attempted by the Commissioner. Petitioner received the dividends in question in fact in 1925 and 1930, respectively. The statute furnishes the sole measure as to when the dividends are to be reported. Under circumstances like those here involved, the First Circuit has held that the dividends are returnable in the year when the dividend checks actually come to hand. (*Commissioner* v. *Adams* (C. C. A. 1) 54 Fed. (2d) 228). The decision in the instant case and in *Shearman* v. *Commissioner* (C. C. A. 2) 66 Fed. (2d) 256, are to the contrary. The decision of the Sixth Circuit in *Commissioner* v. *Bingham,* 35 Fed. (2d) 503, in principle supports petitioner's contention because the decision there was expressly founded upon the special provisions of Section 201(e) of the 1921 Act.

II. The doctrine of constructive receipt is not applicable. The regulations under the 1921 Act embody in the subject of constructive receipt the substance of the provisions found in Section 201(e) of the 1921 Act. Whether such regulations correctly expounded the doctrine of constructive receipt as applied to dividends is immaterial as the regulations simply incorporated the statute itself and the regulations have only such meaning as the statute itself has. Section 201(e) of the 1921 Act did not deal with the question of constructive receipt but declared an arbitrary measure for taxing dividends, separate and distinct from all other items of income. Actual or constructive receipt of the dividend un-

der the 1921 Act was immaterial. It was only necessary that the cash or property should be made unqualifiedly subject to the shareholder's demand. Under the 1921 Act, according to the *Bingham* case, the mailing of the dividend check was relevant only as to the fact as to whether the cash or property was so unqualifiedly subject to the shareholders demand.

The special provisions of Section 201(e) of the 1921 Act were omitted from the 1924 and subsequent Acts. Nevertheless, the Commissioner carried forward into his regulations under these later Acts the same provision as appeared in his regulations under the 1921 Act. The difference now is that such regulations no longer have the express support of the statute. The 1924 and subsequent Acts changed the law as to the reporting of dividends. The regulations issued under these later Acts as here sought to be applied by the Commissioner are therefore void as in violation of the statute. The Commissioner has no power to legislate under the guise of regulations. The essence of the doctrine of constructive receipt is that the fund is actually within the dominion and control of the taxpayer and it is only due to his own voluntary act or conduct that such income is not actually reduced to possession. It is not to be confused with accrual accounting. Here, while the dividends were due on December 31st and petitioner thereafter, if the same were not paid, could maintain an action against the corporation therefor, the corporation chose to make payment by delivery of the dividend checks in such manner as to preclude their receipt by the shareholders until January of the following years respectively. This delay in the transmittal of the dividend checks was not due to the voluntary act or con-

duct of petitioner or of the other stockholders and therefore they cannot be said to have constructively received the dividends prior to the date of their actual receipt when the dividend checks actually came to hand. The cases where dividends and other items of income have been credited to the taxpayer's acaccount upon the corporate books upon which account the taxpayer has the right to draw at will, are clearly distinguishable from cases like the present.

III. The instant case which involves the largest deficiency—$101,269.27—arises under the 1924 Act. Technically, therefore, the *Shearman* case is distinguishable from the instant case as to the latter deficiency for the reason that the *Shearman* case went off on the proposition that the enactment of the 1926 and 1928 Acts (the *Shearman* case involved the 1928 Act) carried with them the regulations issued under the 1924 Act. The rule as to a legislative adoption of an administrative construction of a prior statute does not apply to the same extent or with the same force as in a case like the present where the court is dealing with the 1924 Act itself. Upon the principle, however, applied under certain circumstances, that such legislative adoption of an administrative construction of a prior Act is a legislative approval of that construction of such prior Act the *Shearman* case is probably to be taken as opposed to petitioner's contention. To that extent it is in conflict with the *Adams* case. The court below in the instant cases applies the rule both as to the 1924 and 1928 Acts and to that extent it is also in conflict with the *Adams* case.

The Commissioner may not legislate under the guise of administrative regulations.

ARGUMENT.

I.

THE DIVIDENDS OF $266,490.10 AND $48,984.00 WERE ACTUALLY RECEIVED ON JANUARY 2, 1925, AND JANUARY 2, 1930, RESPECTIVELY, WHEN THE DIVIDEND CHECKS ACTUALLY CAME TO HAND. AS INCOME, THE DIVIDENDS WERE TAXABLE IN SAID YEARS, RESPECTIVELY.

There is no question but that the dividend resolutions under which petitioner received the dividends here involved provided that the dividends thus declared should be payable to the stockholders on or before December 31 of the years 1924 and 1929, respectively. The fact remains, however, that for reasons sufficient to the corporation, and among other things to insure that no stockholder should receive his dividend check until January 2nd, petitioner did not come into possession of his dividends until January of 1925 and 1930 respectively. The legal question is therefore as to whether the dividends, under such circumstances, were "received" by petitioner, under the applicable provisions of the 1924 and 1928 Acts, when in fact received by him through receipt of the checks or were received for tax purposes in the years, respectively, in which the dividends by the resolutions in question were declared to be payable.

There are only three Court of Appeals decisions upon the question arising under the 1924 or subsequent Revenue Acts.

Commission v. *Adams* (1st Circuit), 54 Fed. (2d) 228.

Shearman v. *Commissioner* (2nd Circuit), 66 Fed. (2d) 256.

Avery v. *Commissioner* (7th Circuit) 67 Fed. (2d) 310. (The instant case.)

The *Adams* case involved the 1924 Act, the *Shearman* case the 1928 Act, and the instant case both the 1924 and 1928 Acts.

In addition to the foregoing, the case of *Commissioner* v. *Bingham*, involving the 1921 Act, was decided by the Sixth Circuit—35 Fed. (2d) 503.

The conflict between the various courts of appeal appears from a consideration of the above cases.

The 1921 Act, in Section 213(a) thereof, after defining gross income, provided that the amount of all items of gross income "except as provided in Subdivision (e) of Section 201" should be included in gross income for the taxable year in which *received* by the taxpayer. (Italics ours). Section 201(e) of the 1921 Act provided "For the purpose of this Act a taxable distribution made by a corporation to its shareholders or members shall be included in the gross income of the distributees as of the date when the cash or other property is unqualifiedly made subject to their demands".

In the *Bingham* case it appeared that the corporation had mailed out dividend checks on December 31 and were received by Bingham in January of the year following. He reported the dividends as income for the year in which the dividend checks actually came into his possession. The Commissioner insisted that the dividends were income for the year in which they were declared and payable. The Board, by a bare majority, sustained Bingham's position. (8 B. T. A. 603). The majority attached no especial significance to the provisions of Section 201(e) above and held that the dividends were received when the dividend checks came into the hands of the taxpayer. Some of the dissenting

members were of the opinion that the majority decision wholly ignored the provisions of Section 201(e) and that those provisions were controlling and required a finding against the taxpayer. The Commissioner appealed and the Sixth Circuit Court of Appeals reversed the Board on the ground that Section 201(e) of the Act set up a special rule as to dividends and was controlling. The court expressly pointed out that dividends were specifically excluded from the general provision in Section 213(e) and that the "reason for such exclusion, of course, was that an entirely different basis for fixing the tax year for dividends had already been established in Section 201(e), which section must control". It was further said that "the important thing is that the shareholder did receive a dividend, not when or how. Having received it, the statute (Section 201(e)) required that it be included in his gross income as of the date *not when received* but when the cash (for this was a cash dividend) was unqualifiedly made subject to his demand". (Italics ours). The mailing of the dividend checks was deemed relevant only to the point as to whether the cash or other property was unqualifiedly made subject to the shareholder's demands on the payable date of the dividend and the date when the checks were actually sent out and that the sending out of the checks was sufficient evidence that such cash or property was in fact unqualifiedly made subject to the shareholder's demands. This court denied certiorari.

The whole tenor of the opinion, we submit, indicates that except for the special provisions in Section 201 (e) of the 1921 Act, the decision of the Board would have been sustained.

In the *Adams* case, a similar situation existed as in the *Bingham* case, excepting that the dividend resolution expressly provided that the dividend checks should be mailed out on December 31. The case, as we have said, arose under the 1924 Act. The Board held for the taxpayer, pointing out both the special provision in the dividend resolution there involved and also that Section 201(e) of the 1921 Act had been omitted in the 1924 Act. The Commissioner appealed and the First Circuit affirmed. The court pointed out that the decision in the *Bingham* case rested upon the special provisions of the 1921 Act and that those provisions had been omitted from the 1924 Act. It was said that the 1924 Act did not only not contain the special provisions in the 1921 Act but that in Section 213 (a) it expressly provided that dividends should be included in gross income for the taxable year in which received by the taxpayer. It was further held that the language of the statute was clear and free from ambiguity and that to the extent that the regulations expressed any different rule for reporting dividends they were ineffective.

The Commissioner did not apply for certiorari.

In the *Shearman* case, the dividends were payable December 31, 1928 to stockholders of record at the close of business on that day. Dividend checks were mailed to Mrs. Shearman on December 31 in the usual course of business and after the stock transfer books had been closed. The checks were received in the mail on January 2, 1929. The court said that the *Adams* case was distinguishable because of the special provision in the dividend resolution there involved, and then held that the enactment of the 1926 and 1928 Acts carried with them the administrative

construction of the 1924 Act embraced in the regulations issued under the latter Act and that, therefore, the dividends were to be deemed as "constructively received" in 1928.

Mrs. Shearman did not apply for certiorari.

In the *Shearman* case the Board followed an intermediate decision which was not appealed and which had been decided by the Board before the First Circuit had decided the *Adams* case. (*Re Braxton*, 22 B. T. A. 128.) In the *Braxton* case there was wide divergence of view in the Board.

The instant case was the next and last decision by any Court of Appeals upon the point. As we have pointed out, it involves both the 1924 and 1928 Acts. Technically, the decision in the *Shearman* case is distinguishable, at least as to No. 5029 below which involved the asserted deficiency of $101,269.27 for the year 1924.

The court below in the instant case goes beyond the holding of the *Shearman* case. Its conclusion is that, without more, dividends under such circumstances are income for the year in which they are declared and made payable. The reason given is "that a stockholder of a corporation which has declared a dividend payable before a certain date is on said date entitled to the sum thus declared as a dividend. His right thereto is traceable to the corporate action declaring the dividend, not to the check. The latter merely evidences the liability. It does not create the liability. The date the liability attaches rather than the date of the check which evidences the liability governs". (Tr. 89).

The court thus makes the due date of the dividend the criterion, not the receipt of the dividend by the

stockholder which is the criterion established by the statute. To that extent the court below treats an "accrual" as the equivalent of receipt, although the taxpayer is reporting upon a cash receipts basis. Even the 1921 Act did not make the payable date the sole criterion of taxability, nor do the regulations under the 1924 and subsequent Acts make the payable date of the dividend such criterion. With all deference to the court below, its opinion in this case evidences a confusion of thought as to what is intended by the word "received".

Articles 52 and 1541 of Regulation 65 (1924) and Articles 333 and 621 of Regulation 74 (1928), although there are some differences in phraseology, evidently intend to adopt the substance of the provisions found in Section 201(e) of the 1921 Act. If these regulations are valid as applied by the Commissioner to cases such as the instant case, there being no provision in the 1924 or 1928 Acts equivalent to Section 201(e) of the 1921 Act, then it is a necessary conclusion that Section 201(e) of the 1921 Act was a wholly unnecessary provision. That that section, however, cannot be regarded as surplusage follows, we submit, from the decision in the *Bingham* case and also follows from principle. If Section 201(e) of the 1921 Act was merely intended to provide for the application of the doctrine of constructive receipt to dividends, Section 213(a) of the 1921 Act would be reduced to an absurdity so far as dividends are concerned for it would then read in effect that all items of gross income except dividends are to be reported for the taxable period in which received by the taxpayer but that dividends are to be reported for the taxable period in which constructively received. This construction of Section

213(a) is not only absurd but it would result in the possibility of excluding all other items of income from the doctrine of constructive receipt in accordance with the maxim *expressio unius est exclusio alterius*. That it required no such provision as is found in Section 201(c) of the 1921 Act, to subject dividends to the doctrine of constructive receipt is apparent from *Hadley* v. *Commissioner* (App. D. C.) 36 Fed. (2d) 543 and *Brooks* v. *Commissioner* (4th Circuit) 35 Fed. (2d) 178, both of which cases arose under statutes prior to that of 1921 and subjected dividends to tax upon the theory of constructive receipt upon the same principles as applied to other types of income.

The application by the Board of the doctrine of constructive receipt to the matter of dividends under circumstances like those in the instant case is not only inconsistent with its own views otherwise expressed as to the real meaning and effect of that doctrine, but is obviously colored by a mistaken view of the decision of the Sixth Circuit in the *Bingham* case. It is our view, and we respectively urge, that the decision in the *Bingham* case was correct and in accordance with principle under the 1921 Revenue Act and that the decision in the *Adams* case was correct and in accordance with principle under the 1924 Act wholly apart from the special provision in the dividend resolution there involved. The *Shearman* and the instant cases are contrary to the *Adams* case and contrary, we submit, to the principle recognized in the *Bangham* case.

The 1924 and 1928 Acts tax all income when received, excepting only in the case of other allowable methods of returning income which latter methods

are not involved here. No distinction exists as between dividends and other items of income.

The *Shearman case* gives recognition to the Regulations of the Commissioner to the extent of subjecting dividends to tax upon the basis of constructive receipt where the dividends are payable and the checks are mailed out on December 31st.

The court below in the instant case declares dividends to be taxable as of their due date, without more. In other words, if a dividend is due and payable on December 31 of a given year, the stockholder is obliged to pay a tax thereon, without any regard to whether the dividends are then in fact paid or whether the funds are even then available for payment.

With all due deference, the court below misconceives the essential question. The declaration of a dividend, of course, creates a debt from the corporation to the stockholder. That debt matures upon the day when the dividend is by the resolution declaring it made due and payable, and if the dividend is not paid on that day, the stockholder obviously may maintain an action to recover it. None of this, however, constitutes the receipt of such dividend for tax purposes. Rent or interest may be due during a certain taxable period, but rent or interest is not income *received* merely because due. The only basis on which such items under such circumstances are taxable as income is upon the basis of accrual accounting.

The court below specifically lays aside any question with respect to the mailing of the dividend checks as having any bearing upon the subject with the statement that the right of the stockholder arises

from the declaration of the dividend and not from the check. It is said that the check evidences the liability but does not create it. Obviously, the check is merely the means of paying the dividend or, in other words, discharging the liability. It neither creates nor evidences the liability.

If, therefore, the principle is applied in the taxing of dividends in the Seventh Circuit as laid down by the court in the instant case, then taxpayers in the Seventh Circuit pay a tax upon all dividends as of the year in which the dividends are payable, without any regard whatsoever to whether the dividends are in fact paid or whether the corporation has the means of paying them. Under such circumstances, the taxpayer is taxed, not upon income received, but upon something which he has not yet received.

In the Second Circuit, however, under the principles announced in the *Shearman case,* the taxpayer pays a tax upon dividends for the year in which the dividends are payable only in the event that the funds are then and there available for payment, in which event the mailing out of the dividend check is to be taken as evidence that the funds are so available (compare *Commissioner* v. *Bingham,* C. C. A. 6th, 35 Fed. (2d) 503). In the *Bingham* case the holding is based upon express statute. In the *Shearman* case it rests only upon an administration regulation.

In the First Circuit, under the *Adams case,* however, a taxpayer is not taxed upon dividends until the dividend checks come to hand.

Apart from the subject of accrual accounting, and with the sole exception of the special dividend pro-

visions in the 1921 Act, our income tax laws have taxed income of all kinds upon the basis of receipt.

The 1921 Act also taxed income upon the basis of receipt, excepting only dividends, which were dealt with specially. The 1924 and all of the subsequent Acts tax all income upon the basis of receipt. Such has been the persistent legislative policy.

The Board of Tax Appeals in the instant case expressly stated that its holding in the *Shearman* and other like cases were not in harmony with certain of the language used by the court in the *Adams case*. It was nevertheless of the opinion that it should follow its own decisions and that, with due deference to the First Circuit Court of Appeals in the *Adams case*, it felt that until other Circuit Courts of Appeal had spoken on the question, it should not abandon the view which it had theretofore adopted and followed (Tr. 32-33). It has since adhered to its view. (*Re Peck*, 29 B. T. A. .....; January 23, 1934.)

II.

THE DOCTRINE OF CONSTRUCTIVE RECEIPT IS NOT APPLICABLE.

We have set out in the Appendix the relevant provisions of the various Regulations issued under the various Acts upon the subject of constructive receipt. That doctrine is an administrative concept of the statutory word "received." But, as has been said by the Board (*Re Cowell*, 18 B. T. A. 997, 1001),

> "Unless it is kept within the penumbra of actual receipt, it will invade the field of accrual accounting, and this should not be permitted."

The case of *Re Brander*, 3 B. T. A. 231, is perhaps

the leading Board case upon the subject. It was there said:

> "* * * This doctrine, as we have made clear in several appeals, is not to be applied lightly, but only in situations where it is clearly justifiable. When taxable income is consistently computed by a citizen on the basis of actual receipts, a method which the law expressly gives him the right to use, he is not to be defeated in his bona fide selection of this method by 'construing' that to be received of which in truth he has not had the use and enjoyment. Constructive receipt is an artificial concept which must be sparingly applied, lest it becomes a means for taxing something other than income and thus violating the Constitution itself.
>
> "Doubtless, however, there are clear cases of constructive receipt, such, for example, as that of the bond owner who chooses not to cash his coupon but to permit it to remain uncut in the possession of another. He will not be heard to say that the amount of the coupon is not his income because he did not in fact receive it. The receipt is entirely within his own control and disposition."

Upon occasions, as we have pointed out, dividends have been made the subject of the application of the doctrine of constructive receipt, under circumstances warranting the application of that doctrine. *Hadley* v. *Commissioner*, App. D. C., 36 Fed. (2d) 543; *Brooks* v. *Commissioner*, C. C. A. 4, 35 Fed. (2nd) 178.

In those cases the dividends were actually credited to the stockholder's account upon the corporate books, along with salaries, rents, interest and other items due from the company, and the taxpayer had the right to draw and did draw indiscriminately

against the amount standing in the account to his credit. It would seem apparent that under such circumstances the taxpayer had "received" the dividends for tax purposes.

In the case of the bond interest coupon maturing in a given year, the taxpayer has received during that year, and is in actual possession of, the symbol of the debt, namely, the coupon itself, in which case it may properly be regarded that the income or interest represented by the coupon has been "constructively" received as of the due date of the coupon. Such a case, however, is distinguishable from an ordinary case of interest merely accruing upon a debt which is unpaid. In the latter situation, such interest is not "received" merely because it is past due.

The essence of the doctrine of constructive receipt is that the fund is in fact within the control of the taxpayer and the failure to reduce the fund to actual possession is due to the taxpayer's own voluntary act or conduct. The case of the taxpayer who has a running account with the corporation in which are credited various items of salary, interest, dividends, etc. and upon which account the taxpayer has the right to draw at will, is an example of constructive receipt. Such is not the situation in the present case. Failure to receive the dividend was not due to Petitioner's voluntary act or conduct but was due to the action of the corporation in withholding actual payment until the year subsequent to the payable date of the dividend. Confusion seems to exist with respect to the bearing of the *Bingham* case upon the subject of constructive receipt. That decision did not rest upon any doctrine of constructive receipt but was based upon the special provisions of the Rev-

enue Act of 1921 which made the test of taxability the fact that the cash or property for the payment of the dividend was made available to the shareholder. The mailing of the dividend check there was treated merely as evidence that such cash or property was in fact available on the day the dividends were otherwise payable.

III.

THE COMMISSIONER MAY NOT BY MERE REGULATION CHANGE OR ENLARGE THE CLEAR MEANING OF THE STATUTE.

The applicable statutes state explicitly that all items of income are to be included in the taxable period in which *received* by the taxpayer. The 1921 Act made a special rule as to dividends. That special rule in the 1921 statute was carried into the regulations issued under that statute verbatim. (Arts. 53, 1541; Reg. 62; App. pp. 29-30). Notwithstanding the omission of these special provisions in the 1924 and subsequent acts, the regulations issued in this respect under the 1921 Act were carried forward into the regulations under the later Acts without material change. Obviously, if the 1924 and subsequent acts materially changed the law as to reporting dividends from what it was under the 1921 Act, the regulations under the 1924 and subsequent acts to the extent as here applied, are in direct violation thereof, and are, therefore, void. While administrative construction of a statute may be looked to in order to resolve an ambiguity, resort to such construction will not be permitted to create one. (*R. R. Commission* v. *C. B. & Q. R. Co.*, 257 U. S. 363). Where a statute is free

from ambiguity then administrative construction thereof is immaterial, (*Swift, etc. Co.* v. *U. S.*, 105 U. S. 691; *Iselin* v. *U. S.*, 270 U. S. 245), no matter of how long standing such administrative construction may have been. (*U. S.* v. *Graham*, 110 U. S. 219; *U. S.* v. *Johnson*, 173 U. S. 363).

The *Shearman* case passing upon the 1928 Act held that the enactment of the 1926 and 1928 Acts carried with it the administrative construction of the Commissioner of the 1924 Act. While we do not question the abstract principle thus applied by the Second Circuit in that case and while, under certain circumstances, the re-enactment of the statute may be regarded as a legislative approval of the administrative practice and construction under the prior statute if otherwise reasonable (*Massachusetts Mutual Life Ins. Co.* v. *U. S.*, 288 U. S. 269; *Brewster* v. *Gage*, 280 U. S. 327), the rule is by no means inflexible, and there again, if the statute is clear, the principle does not apply. (*Louisville & N. R. Co.* v. *U. S.*, 282 U. S. 740, 757-9). The First Circuit held in the *Adams* case that there was no such ambiguity in the statute as warranted any administrative construction thereof to the extent attempted in the regulations upon the subject of constructive receipt under the 1924 Act so far as they applied to dividends, or at least to the extent as claimed by the Commissioner in cases like the present.

The *Shearman* case is in conflict with the *Adams* case in this respect and so is the instant case through its approval of the construction and reasoning of the *Shearman* case. In other words, in the First Circuit, the Commissioner's regulations upon the subject of constructive receipt, as applied to dividends, are

void, but are valid in the Second and Seventh Circuits.

Besides the conflict as between the various circuits, the question is a general one involving the construction of the Revenue Acts of 1924 and 1928 and the power of the Commissioner to construe this statute as he has done, questions which should be passed upon and settled by this court once and for all.

We respectfully submit that the writ of certiorari should be granted to the end that upon a hearing the judgment of the Circuit Court of Appeals for the Seventh Circuit should be reversed.

JOHN E. MACLEISH,
LELAND K. NEEVES,
Counsel for Petitioner.

APPENDIX.

1921 Act—Regulations 62.

Article 51. *When included in gross income.*—Gains, profits and income are to be included in the gross income for the taxable year in which they are received by the taxpayer, unless they are included when they accrue to him in accordance with the approved method of accounting followed by him. See articles 21-24; as to dividends, see section 201(e) and articles 1541-1549. * * *

Article 52. *Income not reduced to possession.*—Income which is credited to the account of or set apart for a taxpayer and which may be drawn upon by him at any time is subject to tax for the year during which so credited or set apart, although not then actually reduced to possession. To constitute receipt in such a case the income must be credited to the taxpayer without any substantial limitation or restriction as to the time or manner of payment or condition upon which payment is to be made. A book entry, if made, should indicate an absolute transfer from one account to another. If the income is not credited, but is set apart, such income must be unqualifiedly subject to the demand of the taxpayer. Where a corporation contingently credits its employees with bonus stock, but the stock is not available to such employees until some future date, the mere crediting on the books of the corporation does not constitute receipt.

Article 53. *Examples of constructive receipt.*—When interest coupons have matured and are payable, but have not been cashed, such interest payment, though not collected when due and payable, is nevertheless available to the taxpayer and should therefore be included in his gross income for the

year during which the coupons matured. This is true if the coupons are exchanged for other property instead of eventually being cashed. Defaulted coupons are income for the year in which paid. *Dividends on corporate stock are subject to tax when unqualifiedly made subject to the demand of the stockholder. See section 201 of the statute and articles 1541-1549.* * * * Interest credited on savings bank deposits, even though the bank nominally have a rule, seldom or never enforced, that it may require so many days' notice in advance of cashing depositors' checks, is income to the depositor when credited. * * *

ARTICLE 1541. *Dividends.* * * * *A taxable distribution made by a corporation to its stockholders or members shall be included in the gross income of the distributees when the cash or other propertly is unqualifiedly made subject to their demands. See article 53.*

1924 ACT—REGULATIONS 65.

ARTICLE 50. *When included in gross income.*—Gains, profits and income are to be included in the gross income for the taxable year in which they are received by the taxpayer, unless they are included when they accrue to him in accordance with the approved method of accounting followed by him. See articles 21-24. * * *

ARTICLE 51. *Income not reduced to possession.*—Income which is credited to the account of or set apart for a taxpayer and which may be drawn upon by him at any time is subject to tax for the year during which so credited or set apart, although not then actually reduced to possession. To constitute receipt in such a case the income must be credited to the taxpayer without any substantial limitation or restriction as to the time or manner of payment or condition upon which payment is to be made. A book entry, if made, should indicate an absolute transfer from one account to another. If the income is not

credited, but is set apart, such income must be unqualified subject to the demand of the taxpayer. Where a corporation contingently credits its employees with bonus stock, but the stock is not available to such employees until some future date, the mere crediting on the books of the corporation does not constitute receipt.

ARTICLE 52. *Examples of constructive receipt.*— When interest coupons have matured and are payable, but have not been cashed, such interest payment, though not collected when due and payable, is nevertheless available to the taxpayer and should therefore be included in his gross income for the year during which the coupons matured. This is true if the coupons are exchanged for other property instead of eventually being cashed. Defaulted coupons are income for the year in which paid. *Dividends on corporate stock are subject to tax when unqualifiedly made subject to the demand of the stockholder.* * * * Interest credited on savings bank deposits, even though the bank nominally has a rule, seldom or never enforced, that it may require so many days' notice in advance of cashing depositors' checks, is income to the depositor when credited. * * *

ARTICLE 1541. *Dividends.* * * * *A taxable distribution made by a corporation to its shareholders shall be included in the gross income of the distributees when the cash or other property is unqualifiedly made subject to their demands. See article 52.*

1926 ACT—REGULATIONS 69.

ARTICLE 50. *When included in gross income.*— Gains, profits and income are to be included in the gross income for the taxable year in which they are received by the taxpayer, unless they are included as of a different period in accordance with the approved method of accounting followed by him. See articles 21-24. * * *

ARTICLE 51. *Income not reduced to possession.*—

Income which is credited to the account of or set apart for a taxpayer and which may be drawn upon by him at any time is subject to tax for the year during which so credited or set apart, although not then actually reduced to possession. To constitute receipt in such a case the income must be credited to the taxpayer without any substantial limitation or restriction as to the time or manner of payment or condition upon which payment is to be made. A book entry, if made, should indicate an absolute transfer from one account to another. If the income is not credited, but is set apart, such income must be unqualifiedly subject to the demand of the taxpayer. Where a corporation contingently credits its employees with bonus stock, but the stock is not available to such employees until some future date, the mere crediting on the books of the corporation does not constitute receipt.

ARTICLE 52. *Examples of constructive receipt.*— When interest coupons have matured and are payable, but have not been cashed, such interest, though not collected when due and payable, is nevertheless available to the taxpayer and should therefore be included in his gross income for the year during which the coupons matured. This is true if the coupons are exchanged for other property instead of eventually being cashed. Defaulted coupons are income for the year in which paid. *Dividends on corporate stock are subject to tax when unqualifiedly made subject to the demand of the shareholder.* * * * Interest credited on savings bank deposits, even though the bank nominally has a rule, seldom or never enforced, that it may require so many days' notice before withdrawals are permitted, is income to the depositor when credited. * * *

ARTICLE 1541. *Dividends.* * * * *A taxable distribution made by a corporation to its shareholders shall be included in the gross income of the distributees when the cash or other property is unqualifiedly made subject to their demands. See article 52.*

ARTICLE 331. *When included in gross income.*—Gains, profits, and income are to be included in the gross income for the taxable year in which they are received by the taxpayer, unless they are included as of a different period in accordance with the approved method of accounting followed by him. See articles 321-323. * * *

ARTICLE 332. *Income not reduced to possession.*—Income which is credited to the account of or set apart for a taxpayer and which may be drawn upon by him at any time is subject to tax for the year during which so credited or set apart, although not then actually reduced to possession. To constitute receipt in such a case the income must be credited or set apart to the taxpayer without any substantial limitation or restriction as to the time or manner of payment or condition upon which payment is to be made, and must be made available to him so that it may be drawn at any time, and its receipt brought within his own control and disposition. A book entry, if made, should indicate an absolute transfer from one account to another. Where a corporation contingently credits its employees with bonus stock, but the stock is not available to such employees until some future date, the mere crediting on the books of the corporation does not constitute receipt.

ARTICLE 333. *Examples of constructive receipt.*—When interest coupons have matured and are payable, but have not been cashed, such interest, though not collected when due and payable, shall be included in gross income for the year during which the coupons mature, unless it can be shown that there are no funds available for payment of the interest during such year. The interest shall be included in gross income even though the coupons are exchanged for other property instead of eventually being cashed. Defaulted coupons are income for the year in which paid. *Dividends on corporate stock are subject to tax*

when unqualifiedly made subject to the demand of the shareholder. * * * Interest credited on savings bank deposits, even though the bank nominally has a rule, seldom or never enforced, that it may require so many days' notice before withdrawals are permitted, is income to the depositor when credited. * * *

ARTICLE 621. *Dividends.*— * * * *A taxable distribution made by a corporation to its shareholders shall be included in the gross income of the distributees when the cash or other property is unqualifiedly made subject to their demands. See article 333.*

1932 ACT—REGULATIONS 77.

ARTICLE 331. *When included in gross income.*— Gains, profits, and income are to be included in the gross income for the taxable year in which they are received by the taxpayer, unless they are included as of a different period in accordance with the approved method of accounting followed by him. See articles 321-323. * * *

ARTICLE 332. *Income not reduced to possession.*— Income which is credited to the account of or set apart for a taxpayer and which may be drawn upon by him at any time is subject to tax for the year during which so credited or set apart, although not then actually reduced to possession. To constitute receipt in such a case the income must be credited or set apart to the taxpayer without any substantial limitation or restriction as to the time or manner of payment or condition upon which payment is to be made, and must be made available to him so that it may be drawn at any time, and its receipt brought within his own control and disposition. A book entry, if made, should indicate an absolute transfer from one account to another. Where a corporation contingently credits its employees with bonus stock, but the stock is not available to such employees until some future date, the mere crediting on the books of the corporation does not constitute receipt.

ARTICLE 333. *Examples of constructive receipt.*— When interest coupons have matured and are payable, but have not been cashed, such interest, though not collected when due and payable, shall be included in gross income for the year during which the coupons mature, unless it can be shown that there are no funds available for payment of the interest during such year. The interest shall be included in gross income even though the coupons are exchanged for other property instead of eventually being cashed. Defaulted coupons are income for the year in which paid. *Dividends on corporate stock are subject to tax when unqualifiedly made subject to the demand of the shareholder.* * * * Interest credited on savings bank deposits, even though the bank nominally has a rule, seldom or never enforced, that it may require so many days' notice before withdrawals are permitted, is income to the depositor when credited. * * *

ARTICLE 621. *Dividends.*— * * * *A taxable distribution made by a corporation to its shareholders shall be included in the gross income of the distributees when the cash or other property is unqualifiedly made subject to their demands. See article 333.*

1918 ACT—REGULATIONS 45.

ARTICLE 52. *When included in gross income.*— Gains, profits and income are to be included in the gross income for the taxable year in which they are received by the taxpayer, unless they are included when they accrue to him in accordance with the approved method of accounting followed by him. See articles 21-24. * * * .

ARTICLE 53. *Income not reduced to possession.*— Income which is credited to the account of or set apart for a taxpayer and which may be drawn upon by him at any time is subject to tax for the year during which so credited or set apart, although not then actually reduced to possession. To constitute

receipt in such a case the income must be credited to the taxpayer without any substantial limitation or restriction as to the time or manner of payment or condition upon which payment is to be made. A book entry, if made, should indicate an absolute transfer from one account to another. If the income is not credited, but is set apart, such income must be unqualifiedly subject to the demand of the taxpayer. Where a corporation contingently credits its employees with bonus stock, but the stock is not available to such employees until the termination of five years of employment, the mere crediting on the books of the corporation does not constitute receipt. The distinction between receipt and accrual must be kept in mind. Income may accrue to the taxpayer and yet not be subject to his demand or capable of being drawn on or against by him."

ARTICLE 54. *Examples of constructive receipt.*— Where interest coupons have matured, but have not been cashed, such interest payment, though not collected when due and payable, is nevertheless available to the taxpayer and should therefore be included in his gross income for the year during which the coupons matured. This is so if the coupons are exchanged for other property instead of eventually being cashed. *Dividends on corporate stock are subject to tax when set apart for the stockholder, although not yet collected by him. See section 201 of the statute and articles 1541-1549.* * * *

ARTICLE 1541. *Dividends.*—* * * *The mere declaration of a dividend is not a distribution. Dividends are income and are taxed at the rates for the year in which paid, regardless of when the earnings or profits out of which they were paid were accumulated.*